

STATE OF RHODE ISLAND AND PROVIDENCE PLANTATIONS
PUBLIC UTILITIES COMMISSION

NARRAGANSETT BAY COMMISSION :
ABBREVIATED RATE APPLICATION : DOCKET NO. 3409

REPORT AND ORDER

On December 21, 2001, the Narragansett Bay Commission (“NBC”) filed an abbreviated rate application with the Rhode Island Public Utilities Commission (“Commission”). The proposed rates were designed to generate total revenues of \$45,467,359 and, if approved as filed, would increase NBC’s present revenues by \$8,834,420, or 24.9 percent across the board on tariffed rates for wastewater services. The test year utilized in the rate application was the same as the rate year approved in Order No. 16751.¹ The Commission suspended the effective date of the proposed rate increase at an open meeting on January 12, 2002.

The instant rate case filing represents NBC’s third rate filing in the last eight years. The following table provides a brief history:

<u>DOCKET NO.</u>	<u>DATE</u>	<u>REQUESTED</u>	<u>INCREASE ALLOWED</u>	<u>AUTHORIZED REVENUE</u>
2216	6/27/94	\$8,161,795	\$5,332,025	\$32,098,454 ²
3162	2/29/00	\$10,089,441	\$6,669,489	\$36,632,209

¹ On December 6, 2001, NBC requested that the PUC allow NBC to use the rate year approved in Docket No. 3162 as the test year in their abbreviated rate application. On December 12, 2001, the Division of Public Utilities and Carriers (“Division”) did not object to NBC’s request. At an open meeting on December 13, 2001, the Commission granted NBC’s request.

² The Commission reduced NBC’s annual revenue by \$1,733,272 effective on July 1, 1997.

I. NBC

In support of its filing, NBC filed testimony by Walter Edge, Anthony Simeone, Maureen Gurghigian, Thomas Brueckner and Joseph Pratt. In his pre-filed testimony, Mr. Edge, a CPA and consultant to NBC from Bacon & Edge, P.C., discussed NBC's test year and rate year. Mr. Edge stated that the only two items in this filing are debt service costs and the related debt service coverage required for the next two State Revolving Fund ("SRF") borrowings. Borrowings are needed to fund NBC's Capital Improvement Program ("CIP"), which consists of the Combined Sewer Overflow ("CSO") abatement project and improvements to the Bucklin Point Wastewater Treatment Facility . Mr. Edge used the rate year approved in NBC's prior docket (No. 3162) as the test year for this rate application. He made no adjustments to the test year. For the debt service allowance, which includes principal and interest, Mr. Edge determined that the average debt service cost for all debt (current and proposed) for fiscal years 2003 and 2004 will require additional revenues of \$7,475,786 (a 20.4% revenue increase), consisting of \$4,939,337 in principal and \$2,536,449 in interest. For the debt service *coverage* allowance, Mr. Edge determined that the average annual debt service costs for *SRF-only* financings for fiscal years 2003 and 2004 will require an average coverage allowance of \$3,842,901, or an increase of \$2,158,283 over the debt service coverage allowance currently in rates. However, Mr. Edge proposed to reduce this coverage increase from

\$2,158,283 to \$1,358,634 by utilizing \$799,649 in pay-as-you-go funds presently restricted to capital outlays to meet NBC's debt service coverage requirements. Mr. Edge noted that the overall revenue increase of \$8,834,420 would require an across-the-board increase of 24.9 percent.³ Schedule WEE-10 appended to Mr. Edge's prefiled testimony indicates that a typical NBC residential ratepayer using an average of 100 HCF of water per year would see an annual bill increase of \$40.86, from \$163.99 to \$204.85, or 24.9%.

In his pre-filed testimony, Anthony Simeone, Executive Director of the Rhode Island Clean Water Finance Agency ("RICWFA"), which administers the SRF loans, described RICWFA's zero interest rate loan program developed as a result of the bond referendum approved by the voters in November 2000. Pursuant to the approved bond referendum, the State of Rhode Island issued \$60,000,000 in general obligation bonds in July 2001, of which \$57,000,000 has been designated for wastewater treatment projects. In November 2001, RICWFA closed a \$57,000,000 direct loan to NBC at a subsidized rate of 3.3 percent. In addition, RICWFA has developed a blended loan rate program based on issuing half of the loans at zero percent and half of the loans at a subsidized rate under market conditions. Mr. Simeone estimated that at current market rates, the blended loan rate could be 1.7%, and that some \$276,000,000 in blended rate loans could be made over the next three years. Although

³ NBC Ex. 1: (Edge's testimony), pp. 2-8.

the approved bond referendum entitled NBC to a minimum of \$70,000,000 in zero interest rate loans to fund the CSO abatement project, the blended rate program would entitle NBC to a minimum of \$140,000,000 in blended rate loans.⁴

In her pre-filed testimony, Ms. Maureen Gurghigian, a financial advisor to NBC, discussed NBC's request for funding debt service coverage at 125 percent of principal and interest. Ms. Gurghigian stated that over the next five fiscal years, NBC will be financing a CIP of more than \$364 million. NBC's primary source of capital funding is the SRF program administered by the RICWFA. Ms. Gurghigian noted that since 1999, NBC has had an "A" published credit rating, and that generally, the higher the credit rating, the lower the interest cost to the borrower. According to Ms. Gurghigian, NBC will no longer be allowed to utilize a rolling debt service coverage model; instead, coverage requirements will need to be satisfied on an annual basis to maintain favorable credit ratings. In order for NBC to maintain its favorable credit rating and avail itself of lower interest rates, NBC needs to have rates sufficient to generate coverage for 125 percent of its total debt service on an annual basis. In Ms. Gurghigian's view, without this debt service coverage ratio, NBC's credit rating could be reduced, resulting in RICWFA requiring NBC to pay higher interest rates and/or purchase insurance.⁵

⁴ NBC Ex. 2: (Simeone's testimony), pp. 2-3.

⁵ NBC Ex 3: (Gurghigian's testimony), pp. 2-9.

In his pre-field testimony, Thomas Brueckner, Engineering Manager at NBC, updated the status of improvements to the Bucklin Point Wastewater Treatment Facility (Bucklin Point) and nitrogen removal at Field's Point Wastewater Treatment Facility (Field's Point). The improvements to be made to Bucklin Point will inTdsell

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Brueckner noted that the nitrogen removal project is currently in the “facilities planning stage,” and that once RIDEM issues its new nitrogen effluent limits (currently expected in about one year), the facilities plan would be completed and the design phase of the project initiated.⁶

In his pre-filed testimony, Joseph Pratt, a Vice President of the Louis Berger Group, which serves as NBC’s Project Manager for the CSO abatement project, discussed the status of the CSO abatement project. He noted that the CSO abatement project consists of 13 separate projects that are reflected in NBC’s CIP for fiscal years 2003 through 2007. Mr. Pratt stated that the Moshassuck River Interception Relief (MRI) facilities contract is approximately \$120,000 (2.65%) over budget due to the discovery of higher than anticipated levels of arsenic in the soil and is four weeks behind schedule. Also, Mr. Pratt stated that the Floatable Control Demonstration Facility contract was completed on schedule and on budget. In addition, Mr. Pratt explained that the Main Spine Tunnel contract, which is the single largest component of Phase I of the CSO abatement project, has been awarded to a joint venture, Shank/Balfour Beatty, for \$163,527,245, which is \$12 million lower than the engineer’s estimate for the contract. Mr. Pratt noted that Shank/Balfour Beatty has considerable experience in tunneling. Mr. Pratt stated that the Phase I CSO project costs have been periodically updated and that NBC’s current CIP “reflects costs of \$275 million for all of the CSO related

⁶ NBC Ex. 4: (Brueckner’s testimony), pp. 2-4.

contracts [for Phase I] plus a 10 percent contingency for the CSO construction contracts.”⁷

II. DIVISION

On March 11, 2002, the Division submitted pre-filed testimony by Thomas Catlin and Alberico Mancini. In his pre-filed testimony, Mr. Catlin, a consultant to the Division, discussed NBC’s proposed revenue increase. Mr. Catlin stated that NBC may need to seek additional rate relief prior to fiscal year 2004, because if all debt is issued as currently planned, the total available for debt service and coverage will fall short of 125 percent coverage requirement for fiscal year 2004 (i.e., the 12-month period ending June 30, 2004). In addition, Mr. Catlin supported NBC’s request for Commission approval to allow \$799,649 of funds which are currently restricted to being used only for pay-as-you-go capital outlays to be utilized prospectively first, to satisfy debt service and coverage requirements, and then for pay-as-you-go capital expenditures. Mr. Catlin agreed with Ms. Gurghigian that combining the restricted debt service and restricted capital outlays accounts for this purpose will enable NBC to maintain its favorable debt ratings by satisfying its debt service coverage requirements on an annual basis. Mr. Catlin noted that allowing restricted capital outlays funds to be used to meet debt service and coverage requirements reduced the revenue increase needed to meet NBC’s coverage requirements in the current NBC rate filing by \$799,649.

⁷ NBC Ex. 5: (Pratt’s testimony), pp. 2-6.

He also observed that affording NBC this flexibility in the future will avoid a build-up of restricted funds in the debt service accounts, as well as reduce future borrowing requirements by making all funds not used for debt service available for and restricted to paying for capital expenditures. Lastly, Mr. Catlin stated that NBC's connection permit fees and BOD/TSS surcharge should be subject to the same percentage increase as the rates for other services, thus reducing the across-the-board rate increase from 24.9 percent to 24.8 percent.⁸

In his pre-filed testimony, Alberico Mancini, an engineering specialist for the Division, discussed NBC's CSO abatement project and its various cost estimates. At the outset, Mr. Mancini noted that the Division has been in contact with NBC personnel on a weekly basis. Mr. Mancini stated that the current cost estimate of the CSO abatement project is approximately \$278 million based on final design. He explained that the original cost estimate of \$165 million was provided several years ago and was based on preliminary design. Next, Mr. Mancini explained that the revised cost estimate of \$227 million presented in NBC's prior rate case (Docket No. 3162) was based on 30 percent design, the inclusion of "soft costs," and was based on estimated construction costs in 2004, the mid-point of the construction period, rather than the 1995 construction costs used in the original cost estimate. Mr. Mancini noted that NBC has also added the cost of an

⁸ Div. Ex. 1: (Catlin's testimony), pp. 4-7.

owner's insurance policy (OCIP) to the CSO project cost estimate, as it is required under R.I. worker's compensation law. NBC obtained the maximum amount of insurance, which costs \$14,185,762. In addition, Mr. Mancini stated there has been one change order of \$120,000 relating to the MRI facilities contract. He also stated that the Main Spine Tunnel contract, which was estimated at \$178 million, was awarded for \$164 million, while the MRI facilities contract, which was estimated at \$3.5 million, was awarded at \$4.5 million. As for the RIDOT Land Acquisition contract, Mr. Mancini stated that the land from RIDOT had to be acquired in order to construct the work site at the northern end of the main spine tunnel.⁹

III. HEARINGS

Following duly published notice, public hearings were conducted on April 16 and 17, 2002 at the Commission's offices, 89 Jefferson Boulevard, Warwick, Rhode Island. The following appearances were entered:

FOR NBC: Peter McGinn, Esq.
Tillinghast, Licht, Perkins, Smith &
Cohen, LLP

FOR DIVISION: Leo Wold, Esq.
Special Assistant Attorney General

FOR ATTORNEY GENERAL:¹⁰ Paul Roberti, Esq.
Assistant Attorney General

⁹ Div. Ex. 2: (Mancini's testimony), pp. 2-7.

¹⁰ The Attorney General filed a motion to intervene in this docket. There was no objection.

FOR COMMISSION:

Steven Frias, Esq.
Executive Counsel

At the hearing, Mr. Edge reiterated NBC's request to utilize the pay-as-you-go capital outlays funds for debt service, noting that such a request has been granted for various water utilities.¹¹ Ms. Gurghigian testified that without 125 percent annual debt service coverage, NBC would either borrow less money from RICWFA or receive a lower credit rating so that its borrowing costs would increase. Mr. Edge testified that due to increases in debt service and other NBC operating expenses, NBC would need to file a rate case by the end of 2002 or in 2003.¹²

Mr. Catlin expressed support for NBC's rate increase with the condition that the connection permit fees and BOD/TSS surcharge be increased as well. NBC concurred with Mr. Catlin's modification. Also, Mr. Catlin concurred with NBC's request to utilize the restricted pay-as-you-go capital funds for debt service. Mr. Catlin estimated that in order to pay for debt service, NBC will need another 25 percent increase, and for the next two to four years, NBC will need significant rate increases.¹³

Mr. Pratt testified that the CSO (Phase I) project is currently estimated to cost \$275 million plus a 10 percent contingency, for a total of \$299 million. He stated that the main spine tunnel contract has been awarded to Shank/Balfour Beatty, a joint venture. Responding to concerns expressed by the Commission, Mr. Pratt noted that Balfour

¹¹ Tr. 4/16/02, pp. 10-11.

¹² *Id.*, pp. 26, 32, 49.

Beatty has had legal difficulties, but that the Shank/Balfour Beatty joint venture has not had similar problems and Michael Shank, in whom Mr. Pratt has great confidence, is the managing partner of the joint venture.¹⁴

Mr. Mancini testified that NBC selects the lowest bidder unless there is a bond problem with the bidder or the bid is unreasonable. In addition, Mr. Mancini noted that in the event he disagreed with Mr. Pratt's recommendation to select a bid, Mr. Mancini would bring his concerns to the Commission's attention.¹⁵

In addition, NBC presented Matthew Travers and Camilla Augustine of Parsons Engineering Science, Inc. to discuss their Stormwater Fee Study prepared for NBC.¹⁶ Mr. Travers explained that the Stormwater Fee Study present two alternatives for collecting a user-based stormwater fee. Alternative Model No. 1, the land use model, would cover NBC's entire service territory and assess stormwater fees on all parcels that directly or indirectly contribute *sewerage or stormwater* to the NBC system. Alternative Model No. 2, the modified impervious area model, would only cover NBC's *combined* sewer service territory and assess stormwater fees only to those parcels that contribute *stormwater* directly or indirectly to the NBC system. Approximately 81,000 customers would be assessed a fee under Alternative 1, while

¹³ *Id.*, pp. 67-68, 105, 109-110.

¹⁴ *Id.*, pp. 176, 195-198.

¹⁵ Tr. 4/17/02, pp. 145-146, 149-150.

¹⁶ In Docket No. 3162, the Commission ordered NBC to investigate the feasibility of instituting a user fee based on stormwater runoff to help pay the costs of the CSO abatement project.

approximately 53,000 customers would be assessed a fee under Alternative 2. Both models would assess current NBC customers as well as “free riders.” Both models could be implemented using the existing NBC customer information/billing system, and both are estimate to take about six months to implement. However, there are slightly higher administrative costs for Alternative Model No. 2. Ms. Augustine stated that Parson’s legal counsel had opined that a fee based on stormwater runoff could be imposed by NBC.¹⁷ Mr. Augustine also explained that the purpose of a fee based on stormwater runoff is to recover CSO abatement project costs from those causing the stormwater runoff and the need for a CSO abatement project.¹⁸

COMMISSION FINDINGS

At an open meeting conducted on June 6, 2002, the Commission considered the evidence presented and found NBC’s abbreviated rate application, as modified by the Division’s recommendation, to be just, reasonable, and in the best interest of the ratepayers. In particular, the Commission approved the Division’s recommendation that NBC’s rate increase also be applied to the connection permit fees and BOD/TSS surcharge. Also, the Commission approved NBC’s request to utilize funds restricted for pay-as-you-go capital outlays to meet NBC’s annual debt service and coverage requirements, noting that providing this flexibility will enable NBC to reduce the revenue increase required to

¹⁷ Id., pp. 212-214, 217, 226.

meet debt service coverage requirements by \$799,649. However, any such restricted funds that are not utilized for debt service shall remain available for and restricted to paying for pay as you go capital outlays. The Commission will continue to monitor the costs of the CSO abatement project.¹⁹ Finally, in light of the information presented in the Parsons Stormwater Fee Study Report, the Commission will open a separate docket to explore in greater detail the feasibility of implementing a user fee based on stormwater runoff to assist in paying for the unprecedented costs of the CSO abatement project.

On July 10, 2002, NBC filed its compliance tariffs reflecting the Commission's open meeting decision in this docket. On July 17, 2002, the Division filed a memorandum recommending approval of NBC's compliance tariffs as filed. At an open meeting on July 18, 2002, NBC's compliance tariffs were reviewed by the Commission and unanimously approved.

¹⁸ *Id.*, pp. 244-245.

¹⁹ NBC appealed the Commission's Order in Docket No. 3162, Order No. 16751 (issued October 25, 2001), challenging the Commission's right to order NBC to restrict \$150,000 annually from its 1.5% operating reserve to fund an independent overseer to monitor the progress and costs of the CSO abatement project for the benefit of NBC's ratepayers. As of the date of the Commission's open meeting decisions in this docket, NBC's appeal was still pending before the Rhode Island Supreme Court. However, the Commission notes that on November 1, 2002, the Supreme Court rejected NBC's challenge and affirmed the Commission's right to engage an independent overseer to monitor the CSO project and to require NBC to pay for these services. See Narragansett Bay Commission General Rate Filing, No. 01-518 (November 1, 2002).

Accordingly, it is

(17304) ORDERED:

1. The abbreviated rate application filed by Narragansett Bay Commission on December 21, 2001, as modified to include increases in the connection permit fees and BOD/TSS surcharge, thereby resulting in an across-the-board rate increase of 24.8 percent, is hereby approved.
2. Narragansett Bay Commission shall be permitted to use \$799,649 of funds restricted for pay as you go capital outlays to satisfy annual debt service and coverage requirements, provided that any such funds not used for this purpose shall remain available and restricted to paying for pay as you go capital outlays.
3. The compliance tariffs filed by Narragansett Bay Commission on July 10, 2002 are hereby approved.
4. Narragansett Bay Commission shall comply with all other findings and instructions contained in this Report and Order.

EFFECTIVE AT WARWICK, RHODE ISLAND PURSUANT TO OPEN MEETING DECISIONS ON JUNE 6, 2002 AND JULY 18, 2002. WRITTEN

ORDER ISSUED DECEMBER 17, 2002.

PUBLIC UTILITIES COMMISSON

Elia Germani, Chairman

Kate F. Racine, Commissioner

Brenda K. Gaynor, Commissioner